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ABSTRACT

This document contains the proceedings of a conference dealing with the issues that face U.S. cities today. Convened in October of 1979, the conference was sponsored by the Federal Reserve Bank of Philadelphia. The document contains addresses and comments by six authorities on the current fiscal situation of large cities. The presentation "America's Cities" recounts urban America's development and outlines a program for the recovery of urban America from its afflictions of ugly slums, disgraceful housing, ineffective schools, violent crimes, malnutrition, drug abuse, and widespread human suffering. Included in the recovery program is federal recognition and responsiveness; the stabilization and rebuilding of cities' economic bases to be competitive in terms of business, industry, and commerce; the curtailment of spending; and the rejuvenation of neighborhoods. The second presentation "The Future of Large, Older American Cities to the Year 2000" examines trends which include a lack of housing demand in cities and the conflict between suburban growth and city restoration. Commenting on the second presentation, the third speaker states that to help solve city problems government should stimulate the marketplace rather than invest in large public works programs. Leadership and risk taking are needed. All of us have a role to play in reactivating our own ingenuity in using cooperatively both private and public resources. Two of the presentations deal with "The Fiscal Stance of Philadelphia." The concluding presentation examines "The Changing Nature of Intergovernmental Relations." (Author/RH)

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THE FUTURE OF AMERICAN CITIES

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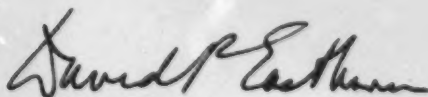
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FOREWORD

The Federal Reserve Bank of Philadelphia has an ongoing interest in the economics of urban life. Over the years, the Bank's Department of Research has published many studies on the issues that face cities and regions, especially those that bear directly on the economic and financial vitality of the Philadelphia region.

Last October, as part of the nation's Bicentennial observance, we brought together several leading authorities on the current fiscal situation of large cities. Our first speaker, Mayor Bradley, gave us an inspirational and hopeful message. During the afternoon sessions, Mrs. Summers and Messrs. Downs, Meyerson, Moak, and Raiff offered us a close look at some of the bread-and-butter issues. And Secretary Hills capped the day with a review of current Federal initiatives.

The addresses and comments printed here are the proceedings of that conference. I hope that they will lead to a better understanding of some of the economic factors that underlie basic urban policy alternatives.



David P. Eastburn
President,
Federal Reserve Bank of Philadelphia

THOMAS BRADLEY

Thomas Bradley, Mayor of Los Angeles, served in his city's Police Department for 21 years. He was admitted to the California State Bar in 1956 and, upon retirement from police work in 1961, entered private legal practice. He began 10 years on the Los Angeles City Council in 1963, ran unsuccessfully for mayor in 1969, and won that office in 1973.

Mayor Bradley is past president of the National League of Cities and current chairman of that body's advisory committee. He is past president also of the National Association of Regional Councils, a director of the California League of Cities, and a member of both the United States Conference of Mayors' Legislative Action Committee and the National Committee on Productivity and Work Quality.

America's Cities

The Honorable Thomas Bradley
Mayor of Los Angeles

For more than three decades now, I have spent my life learning about city living and government in Los Angeles—as a police officer, as a city councilman, and for the last three years as mayor. City life has been my chosen life-style, and its preservation has been my chosen life's work. My concerns have been and always will be the concerns of America's cities.

In recent years our attention—the country's attention—has been so preoccupied with the problems and tragedies of America's cities that we often have failed to see their great strengths. In fact, urban America in the 1970s could be summed up as a tale of two cities. America's cities represent the best and the ugliest that our society has to offer. In them we see pinnacles of American culture. We see vibrant centers of world commerce and industry. They are great gathering places of our people—the nerve centers and marketplaces of 20th-century America.

Our cities are powerful, they are fascinating, they are cosmopolitan, and most of all they are home for three-quarters of this country's population. Yet in the shadow of this greatness lies much of the shame and despair of America—ugly slums, disgraceful housing, ineffective schools, violent crime, malnutrition, drug abuse, and widespread human suffering. These are in stark contrast to the grandeur and splendor that often stand only a few short blocks away.

As our third century begins, we, as a nation, need to commit ourselves to the recovery of urban America. But before I talk about the focus and substance of this recovery agenda, I want to put things somewhat in perspective by briefly recounting urban America's development.

In the 1600s, British and Dutch pioneers founded five villages along the eastern coast. They were destined to grow into our first cities: Boston, Philadelphia, New York, Newport, and Charleston. The combined effects of the industrial revolution, massive immigration from Europe and the Far East, the railroads, and abundant natural resources created unprecedented growth in the number of cities. Cities became the heartbeat of the nation. They became the centers for people looking for a better life. They have been the great depositories of wealth and opportunity of this century. Legends of quick riches attracted the hopeless, the star-struck, and the ambitious.

At first, the cities seemed up to the challenge of ingesting this rapid influx. Revenue sources looked plentiful and the economy was booming—except for an interruption which history calls the great depression.

When people started making more money, they started developing the collective tendency to be a disposable society, using things and simply tossing them away—everything from disposable cans and bottles to throwaway lighters and razors. In the last 20 years, this throwaway lifestyle has overtaken even our cities, particularly older communities: the idea is to get out fast and not look back.

The more affluent people and businesses often left the aging city cores and moved to newer, greener-looking suburbs tied to the market and theatre centers only by ropes of superhighways and train tracks. There they could watch what was happening to the old neighborhoods on television, from their remote vantage points in the country. Left behind in the 1960s and 1970s were slums, abandoned housing, factories, offices, graffiti-covered walls, and people on the lower end of the economic scale—the ones who couldn't afford to get out.

New York is the classic example of this deterioration because of the magnitude of its problems and the publicity surrounding them. But by no means is it unique among American cities. You have seen the great battle of the budget happen here as well. Though thankfully on a lesser scale, it has happened and it is happening in big cities and small all across the country. No city in America is safely outside the reach of financial peril. In fact, the U.S. Conference of Mayors recently completed a survey of municipal governments' financial conditions. Only 21 of 136 cities—only about 15 percent—could say that their governments were not in immediate trouble.

Yes, the condition of American cities—old and young, big and small—is serious in medical terms. But there are hopeful signs that point to a healthier prognosis. The requirements for an urban recovery are as clear as they are compelling:

First, federal recognition and responsiveness are essential. Policies and programs which either directly or indirectly contribute to deterioration must change.

Second, cities must stabilize and rebuild their economic bases to be competitive in terms of business, industry, and commerce. The importance of this is shown by the fact that New York has lost 500,000 jobs in the past five years, and San Francisco and Philadelphia, proportionately, have been losing as many. It should be the other way around. We should be producing that many jobs.

Third, city officials—and the public—have to curtail spending appetites and constantly evaluate the quality and the cost-effectiveness of municipal services. This means making hard decisions based on hard realities. Often this means acting in opposition to tremendous special interest pressure.

And fourth, neighborhoods have to be rejuvenated through reinvestment to make them better able to compete with suburbs. In short,

city government has to become more personal, more prudent, and more productive.

These are tall orders, but I think they are attainable goals. They require the application of the fundamentals of sensible, good government that is in tune with the times. This goes for newer, growing ones, as well as for older cities.

What does all this mean in practical terms? Perhaps I can explain best by telling you what is happening now in Los Angeles, how we are trying to prepare for the future by minding what we do today.

Los Angeles is operating within the framework of a fiscal philosophy that I like to call enlightened stinginess. By that I mean we take nothing for granted. Everything the city does has to undergo strict evaluation as to its effectiveness in meeting clearly defined objectives. Its financial consequences and the economic impact on taxpayers must be considered. There is no automatic renewal of programs, no matter how traditional they have become. With all the demands for more services, it has been made clear that there will have to be some sacrifices all around.

In the past three years, over \$200 million has had to be cut from city department requests. This has meant that some programs have had to be shaved and some others eliminated altogether.

One very tangible result of this kind of pinchpenny philosophy is three years of balanced budgets without new taxes. This year even had a 10-percent reduction in the city's property tax rate.

We are improving Los Angeles' business climate, also. Some of the country's most outstanding leaders from labor unions, industry, finance, law, and academic circles are working side by side on active citizen committees to help the economic development program of the city. Among the projects they have undertaken already are: attracting new business to Los Angeles and keeping that which is already there; eliminating regulatory red tape and unnecessary delays; investigating the financial condition of city government and suggesting ways to improve it; promoting investment in decaying neighborhoods; and increasing foreign trade.

The goal of all this activity is two-fold: first, to create better business opportunities; second, and most important from my viewpoint, to generate more job opportunities to relieve the human hardship caused by unemployment.

I mention the example of Los Angeles only to illustrate the broad approach which has to be taken by cities to reverse their downward spiral.

As a leader in your community, each of you can contribute greatly in the common struggle to salvage city living as a viable life-style. In a nutshell, we need you, your talent, and your energy.

A few minutes ago, I mentioned the Federal government and its vital role in the recovery. Because of the tremendous impact the Federal government has on us, individually and collectively, its participation and cooperation are critical to the success of reviving urban America. I

believe a well-rounded national policy, or collection of policies, must be set forth—not to save one city, not to save a dozen cities, but to redeem the future of our major metropolitan areas which are linked so closely to the future of this nation and its survival.

Let me preface my remarks about the Federal role with some given principals. Government at all levels will have to become more innovative in the way it does business. We must operate with the understanding that taxpayers' money is not an infinite resource which can be tapped at will. Since government will have little new money from which to draw in years to come, we are going to have to tune its operation carefully and improve its performance in everything from streetcleaning to education, from national defense to public protection. That means government will have to make better use of what it already has, and it means that it must somehow maintain top-quality service by finding ways of doing it for less.

In short, it must follow some basic business principals: (1) it must improve the productivity of its workers, (2) it must realign priorities to reflect current realities, and (3) it must move to improve the effectiveness and efficiency of services through consolidation and by streamlining delivery procedures.

In the Federal government I believe it means that serious consideration should be given to the development of an integrated Federal economic development and revitalization program. This concept could meet the different needs in various urban areas of the country by pulling together current manpower programs, housing and community development programs, transportation and economic development programs. The approach would promote flexible and innovative means of dealing with some of the more highly complex and interrelated problems.

The potential savings from integrating such policies as transportation and urban development look impressive. For instance, if the average length of home-to-work trips were reduced only one mile each way for the 50 million automobiles used daily for commuting, total travel per year would be reduced by 25 billion vehicle miles, a saving of 1 million barrels of oil a week.

Earlier I mentioned an agenda for urban America which should become the cornerstone of national policy decisions during the beginning of the third century of our nation.

From this day forward we, as a nation, must commit ourselves to the goal of full employment—a job for every man or woman who wants to work. We must commit ourselves to the goal of comprehensive welfare reform. We must commit ourselves to the goal of adequate, affordable housing, of ridding our cities of violent crime, of better health care, and of more effective education that is available on an equal basis.

These are some of the more basic elements of the urban recovery agenda. But above and beyond these, there are several other fundamental shifts in strategy which require cooperation of the Federal,

state, and local governments. I have seen anger and frustration in the faces of many people who are unable to keep up with the demands of antiquated, counterproductive property tax policies.

What's needed is an overall tax system which encourages property tax reform and relief and reinvestment in cities. It should be a functional tax system which recognizes that property taxes were intended to pay for services related to property, such as police and fire protection, street work, sewers, and garbage collection. Incentives should be given to states that undertake property tax reform to discourage flight of families out of cities. Tax reform should reduce the trend of imposing severe hardships on many low-income, middle-income, and elderly persons who make up the major portion of urban populations—those who can least afford to pay.

Additionally, I think we need changes in the Federal tax system to encourage more urban investment, including selective tax-investment credits for urban redevelopment and for middle-sized and small urban businesses.

The last and perhaps the most crucial part of the recovery equation is to coordinate Federal, state, and local policies which have a bearing on revitalization and resettlement in metropolitan areas. Tax credits, low-interest loans, and specialized grants could be utilized to encourage businesses and homeowners to relocate in cities. Both the National League of Cities and the U.S. Conference of Mayors are making urban neighborhood conservation and reinvestment one of their top priorities. This was a major policy action of the NLC during my term as president in 1974.

In order to avoid the pitfalls of past programs which may have been well-meaning but which literally threw away millions of dollars with little to show for it, I would propose that any national urban recovery program have one string attached. Priority for Federal assistance should be given to those areas which are willing to adopt and pursue clearly defined recovery programs that show tangible results. This was the philosophy behind the rebuilding of Europe after World War II, and it was unmistakably successful.

Problems faced by new expanding cities and by older ones really can't be separated at this point. They are so similar and so massive that no single leader or law or party, no simple slogan or dramatic act, can, by itself, set things straight. But I do believe a concerned, continuing effort by responsible leaders from every section of society to explain the complexities of decisions, to put expectations in proper perspective, to bring people back into the process of evaluating alternatives, even to admit indecision in the absence of evidence and to promise only that which is realistic, can hasten the recovery.

The cities' plight clearly cries out for attention and for bold, progressive leadership from government and from the private sector as well. Working together I believe we can make America's cities the envy of the world once again.

ANTHONY DOWNS

Anthony Downs combines his board chairmanship at Real Estate Research Corporation with a busy schedule of consulting assignments in and out of government and occasional lecturing at some of the nation's leading universities.

Trained in political theory and economics at Carleton College and Stanford University, Mr. Downs is the author or coauthor of several books and many articles on urban affairs. He wrote the Committee for Economic Development's report on the urban poor as well as the United States Civil Rights Commission's report on racism in America.

Mr. Downs is a trustee or director of five Chicago-area civic organizations and serves on the advisory boards of the Institute for Research on Poverty and the National Bureau of Economic Research. He was a member of the National Commission on Urban Problems and now acts as a consultant to the Urban Institute.

The Future of Large, Older American Cities to the Year 2000

Anthony Downs
Real Estate Research Corporation

I. INTRODUCTION

It is indeed challenging to consider what the future of American cities will be like to the year 2000. However, I have always disliked the term 'cities' as it is so often used today. Technically, it covers every hamlet of more than 2,500 people, including all affluent and poor suburbs, as well as the major large and older central cities which Northeasterners think of when they hear that term. To reduce this ambiguity immediately, I am going to speak primarily about large, old central cities in the Northeast and Midwest, most of which contain sizable minority-group populations—like Philadelphia.

II. MAJOR CHANGES DURING THE PAST 24 YEARS

Let me begin by looking backwards the same 24-year timespan as 2000 is from today—to the year 1952. That will give us some idea of the degree of change likely to occur in such a timespan in our society.

The first thing that strikes me is the tremendous continuity of our society over the past 24 years. No really radical changes in our urban settlements have occurred. We are not commuting by rocket belts, or being served by robots, or living in earth satellites. Similar continuities will persist in the next 24 years too.

On the other hand, in relation to cities as I have narrowly defined that term, some important changes have taken place since 1952. Moreover, some of them have become ongoing trends that are likely to continue into the near future, or beyond.

The rate of U.S. population growth changed quite remarkably in this period. It first rose very rapidly through a period of many births from about 1954 to 1964, and then fell even faster to our present very low fertility rates. The current trend is toward much slower overall population growth rates, even though we are in a period when large numbers of households are being formed each year.

DOWNNS

A second major change since 1952 has been the dominance of urban growth by the suburban portions of metropolitan areas. The rapid spatial expansion of suburbs has been based upon a virtual explosion of automobile ownership and use, the building of major highway networks out of and around large cities, and high levels of suburban housing construction—most remarkably in the super-boom in real estate in the early 1970s up to 1973.

In 1952, there were about 54.6 million cars, trucks, and buses registered in the U.S. Today, there are 135 million such vehicles registered—a stupendous rise of 80 million vehicles while our total human population went up 57 million. Moreover, the vehicle population is now rising about 5 to 6 million per year, as compared to the human population increase of about 1.5 million. If these two growth rates continue, by the year 2000 we will have a vehicle population of 279 million, 10 percent above today's, and a human population of 251 million—or 1.1 vehicles per person.

A key aspect of massive suburbanization of our population has been the inclusion in suburban growth of all types of activities, not just housing. Suburbs now contain every type of employment and service, from retailing through office space and industry to medical services and universities.

A third change since 1952 vital to large cities has been the loss of population and activity sustained by many such cities, as both shifted to suburban areas and—lately—outside metropolitan areas. From 1960 to 1970, 56 of the nation's 153 cities containing over 100,000 people lost population. But from 1970 to 1973, 87 of those cities lost population—including 26 out of the 28 in the Northeast, and 29 out of 41 in the North Central or Midwest region.

The people leaving these cities have been among the more affluent former residents. That has raised the proportion of relatively low-income and minority-group persons left in large cities, as compared to their suburbs. These losses of population have in some cases accompanied serious losses of economic functions, as major employment centers also moved out of cities. Whole neighborhoods have become abandoned in some cities, losing large fractions of the population that resided there in 1952. The result has been a major *fiscal squeeze* on the budgets of big-city governments, as you know.

The magnitude of population losses in some large U.S. cities since 1950 is rather startling. From 1950 to 1973, St. Louis lost 35 percent of its total population; Cleveland lost 26 percent; Detroit lost 25 percent; and Pittsburgh lost 29 percent. Philadelphia lost only 10 percent—but that was 210,000 people.

A fourth major development since 1952 relevant to large cities has been the evolution of Federal urban-oriented programs. We went from a period of mainly suburban-construction-oriented programs (in the 1950s) through major emphasis upon urban-aid programs. Examples are urban renewal, the antipoverty program, the model cities

program, and expensive subsidized housing aids. These were prominent in the late 1960s and early 1970s. Since then, we have shifted to what might be called a two-pronged Federal transfer-payment strategy. Instead of designing specific programs to aid cities, we give them money directly in the form of revenue sharing and indirectly by transfer aids to their residents through welfare, unemployment compensation, food stamps, and health programs.

III. CURRENT AND FUTURE TRENDS AND BACKGROUND FACTORS

Now that I have looked back 24 years, let me turn to describing certain key background factors, forces, and relationships that are going to influence the future of cities in the next 24 years. Some of them are continuations of the trends I have just mentioned.

A. Lack of Housing Demand in Cities. First, the continued slowing of population growth in the nation, combined with more-interregional migration away from the Northeast and Midwest to the Sunbelt, means that more and more entire metropolitan areas in the Northeast and Midwest will be experiencing very low total population growth or outright losses of population. This means further weakness in older neighborhoods and more housing abandonment, at least in the absence of any countervailing factors likely to raise housing demand there.

There are only two major possible sources of new demand for central-city housing under these conditions. One is *small adult-oriented households*, since children will be of decreasing importance in future household life. We are already seeing a rapid increase in the number of small households. They are more oriented towards in-city life than the child-oriented households which dominated past population growth.

The other major possible source of housing demand for central cities could be a *new wave of low-income immigrants*—especially from Latin America. Such a wave is already entering many cities illegally. We will be facing a sharp drop in new entrants to the labor force around 1985; so we may even deliberately open up immigration to solve a future labor shortage. After all, housing abandonment is partly a result of the absence of any new inflow of poor migrants needing economic and social upgrading, since the flow of such immigrants from the Southern mechanization of agriculture stopped in the late 1960s.

This possible future shift would intensify slum housing conditions in our larger cities. It would not solve their housing problems through upgrading, but would put an end to abandonment. However, I doubt if we will do this deliberately, because the high wage levels of American labor are based upon a hidden foundation of preventing really large-scale inflows of cheap labor from abroad.

B. The Conflict Between Suburban Growth and City Restoration. The second key factor relevant to future city conditions is the conflict

DOWNS

between continued suburban growth and expansion on the one hand, and the restoration or rebuilding of older central cities on the other hand. Clearly, the *sine qua non* of big-city population losses has been massive building of housing and other facilities in surrounding suburbs. These newer, more attractive facilities were located in neighborhoods free from poverty because of exclusionary zoning. They have drawn millions of middle-income and upper-income households out of older cities. The more new housing and other facilities we create in suburbs in the future—as in the past—the more we will depopulate older city neighborhoods—especially causing them to lose people with good incomes.

Far from having a housing shortage, we built so many housing units in the early 1970s in most metropolitan-area suburbs that this accelerated the loss of people from big cities, as shown by the data cited earlier. Thus, there is a direct conflict between achieving high levels of new total housing production—as advocated by the building industry, academic housing experts, and construction unions—and the improving economic health of older central city governments. That health would be best served by an acute national housing shortage raising the demand for older housing units.

Many so-called urban experts believe our society needs strong and vital central cities in order to survive. I doubt it. If our central cities lose vitality, it may cause some change in our spiritual life—perhaps even a change for the worse. But it will hardly cause us to disappear or our civilization to end. The doughnut can live quite well without the hole being occupied with vital activities, in my opinion. It is already doing so in some areas.

Thus, the level of total national housing production will have a crucial impact upon older cities in the future. The lower it is, the better for them, at least in terms of their economic and fiscal viability. Total housing production in turn depends mainly upon general economic conditions. Therefore, the general economic climate is the key to the strength of future housing demand in older cities. The greatest likelihood is for continued business cycles, which will contain sufficient periods of high-level or medium-level total new housing output to further weaken older cities. This will benefit consumers, however, since they clearly lose from the high prices typical of housing-shortage conditions.

Another facet of the suburban-central city conflict concerns political strength in the national Congress and state legislatures. As suburbs grow, they gain more such strength and are less and less likely to support programs of specific aid for older cities. This is clearly shown by the strong national hostility to New York City and its fiscal crisis. Hence I consider major programs of Federal aid for big-city restoration less and less likely to be adopted as time passes, unless they are parts of aid programs providing sizable benefits to other areas too.

One possible political alliance helpful to older cities would be between their governments and suburban antigrowth advocates, who want to keep low-income residents out of suburban areas. If central

cities allied with antigrowth suburbanities to slow down all suburban growth drastically, national housing shortages would be created. They would strengthen housing demand in central-city neighborhoods and improve property values and tax bases there, although they would also harm poorer residents because of higher housing costs.

C. The Negative Triple Whammy. A third major factor influencing the future of large cities is what I will call the Triple Whammy of negative forces from which many such cities suffer. This trio of factors makes it extremely difficult to visualize any resurgence of dynamism in many of their neighborhoods where abandonment and decay have begun.

The first factor is racial segregation of housing markets. It leads to spatial concentration of low-income minority-group households in poverty-dominated central-city areas where housing is old and deteriorated. Middle-income persons of all races—especially whites—simply will not move into such areas, with the rare exception of young white households rehabilitating very well-located older neighborhoods. Because of both racial and economic segregation, the concentration of these low-income and minority-group households in older cities causes whites to withdraw elsewhere. Regardless of widespread mayoral rhetoric, those households cannot be lured back into such cities as long as poverty concentrations remain there. It is even possible that future minority-group dominance of downtown business districts—already true of retailing in many—may cause withdrawal of white office-work employers from older city CBDs. This has already happened in Detroit and Newark and St. Louis to some degree.

Equally serious, a whole generation of dispossessed young blacks without proper family stability, school education, or employment opportunities is now growing up in large central cities. This group is responsible for a disproportionate share of crimes, vandalism, and insecurity in such cities. We simply do not know how to cope with them in ways that are either humanitarian or effective. Our major response so far is for all groups that can avoid them to withdraw somewhere else. Until the black community itself develops some internal control and discipline over this group, it is hard to see much improvement occurring. But how can the black community do that without money and with only low-level employment opportunities open to many of its members?

The second factor in the Triple Whammy is the obsolescence of the stock of housing, factory buildings, store buildings, streets, and other physical structures and improvements in central cities. They simply cannot compete with newer facilities in suburbs—or other regions—in attracting households and firms with money. Moreover, under the conditions of vandalism and labor-force difficulties common in large cities, rehabilitation is no cheaper than new building in suburban areas that contain far more attractive environments and amenities.

The third factor in the negative Triple Whammy is the high cost structure of both public-sector and private-sector operations in older cities. This results from the presence of strong unions—both public and private, very high levels of public services, high wages and fringe benefits, and the high tax-costs of dealing with dependent low-income populations. Economic entities that are cost-conscious—whether households or business firms—are driven to shift to other locations with lower costs, especially in the South and West. Costs are now lower there because union strength is far less, wages are lower, public services are less extensive, and welfare benefits are at very low levels.

D. Some Limitations of Public Policy. The last background factor I want to discuss concerns the limitations that affect our ability to intervene in, or change, ongoing trends through public policies. At least three such limitations are worth mentioning briefly.

One is our limited ability to manage complex governmental operations, especially those which require coordination of many different types of actions, such as housing, code enforcement, education, and criminal justice. Because the goals of public managers of social programs are far more diffuse and vague than those of profitmakers, we are simply incapable of coordinating any really complex social programs very effectively—as experience proves so clearly.

This is related to the second limitation—our unwillingness to enforce any type of social rules that require real discipline or harsh action, or cost much in terms of money. For example, our welfare agencies simply cannot enforce the rules of eligibility. Either the workers don't want to, or they are unable to. We are unwilling to cope with crime by jailing criminals for long periods because it would be too costly in terms of both building much bigger jails or restricting civil rights. Therefore, future solutions that require rigorous enforcement of rules won't work, unless we are more willing to change our permissive cultural attitudes than we have been until now.

The third limitation is that our elected officials will not confront the need to say No to any group, even under conditions of very limited resources. We have no true national growth policy because it would require Congress to indicate some areas should grow more than others—and it refuses to do that for political reasons.

All these limitations, and others, mean that many theoretically effective ways of attacking big-city problems cannot work in reality.

IV. THE FUTURE OF U.S. CITIES

Now that I have expounded at length about background factors, what can I say about the future of the large cities we are considering, between now and 2000? There are really two key aspects of such future developments: *residential* and *employment*. Although they are closely related, I will focus mainly upon the residential, and then make just a few comments about the employment aspect.

A. Possible Residential Futures. What future strategies could we

adopt concerning large cities as places to live, in light of the factors already discussed? I have conducted a complex analysis of all the possible future combinations of five major *residential policy variables*. There are at least 32 such combinations, but I have narrowed down those possibilities to a mere eight alternative strategies. The five policy variables are the annual levels of: (a) total *national* new housing production, (b) demolition of older units within cities, (c) relocation of households within cities, and (d) rehabilitation of older units within cities, and also (e) the location of new housing—either entirely in suburbs or partly in cities. I will not attempt to spell out the complexities of how I got down to only eight strategies, but I think they cover the reasonable possibilities rather thoroughly. These eight strategies and their relations to the above policy variables are shown in the accompanying table.

FIVE KEY ELEMENTS OF ALTERNATIVE FUTURE RESIDENTIAL STRATEGIES

Alternative City Residential Strategies	Level of Total National Housing Production	Location of New Housing Units Built	Annual Level Within Large Older Cities of—		
			Housing Demolition	Household Relocation	Housing Rehabilitation
Core Obsolescence and a Tight Market	Low	Mainly in Suburbs	Low	Low	Low
Roll-over Rehabilitation	Low	Mainly in Suburbs	Low	Low	High
Core Clearance Only	High	Mainly in Suburbs	High	High	Low
Core Clearance Plus Rehabilitation	High	Mainly in Suburbs	High	High	High
Core Clearance Plus Rebuilding Only	High	In Both Cities and Suburbs	High	High	Low
Core Clearance Plus All-Out Renewal	High	In Both Cities and Suburbs	High	High	High
Residential Core Abandonment	High	Mainly in Suburbs	Low	High	Low
Residential Core Upgrading	High	In Both Cities and Suburbs	Low	High	High

DOWNS

Only two of these eight alternative strategies are low-annual housing production strategies. They do not allow much movement of households out from central cities because not enough suburban housing is being created through new production. One of these is *core obsolescence with a tight housing market*, or what can be called *slum preservation*. It involves low housing production, mainly in the suburbs, with low demolition, rehabilitation, and relocation within cities. Little rehabilitation or demolition is carried out in cities because there is no place for the households who would be displaced by demolition or rehabilitation to move. Also, there is no public financial housing assistance for the poor, who cannot pay the higher cost of rehabilitated units without such assistance. Hence the poor can continue to be housed only if existing slums are neither torn down nor upgraded, but preserved as they are! Some cities embody this strategy now.

The second low-production alternative is like the first except that it involves high-level rehabilitation within older cities. But since there is no place to put the households displaced by rehabilitation during upgrading, all rehabilitation must be tightly administered in what I call a *roll-over rehabilitation* process. In it, people move out of one set of units to be rehabbed directly into another set where rehab has already been done. This requires both extremely complex administration and large-scale income subsidies to the poor so they can afford to live in rehabilitated housing.

Four other possible strategies involve high enough total housing production each year to allow major clearance of older units in core areas. Such new production is necessary because core clearance involves the displacement of lots of households. The displaced households do not need to move directly into new suburban units, but enough new units must be built to loosen up the entire inventory so displacement can be accommodated somewhere. The *core clearance* alternatives vary concerning what is done in the cleared areas. It can be just clearance, leaving vacant space; or rehabilitation of non-cleared areas; or rebuilding of new housing in the cleared areas in wholly new environments (thus large-scale projects); or what I call all-out renewal—both new construction and rehabilitation.

The last two alternatives for city housing involve both high-level new production and low-level demolition within the large cities themselves. One is *residential core abandonment*—just continuing the shift of population to new suburban units without any real improvement or clearance of abandoned areas. The other is *residential core upgrading* by inserting some new units into abandoned areas and doing major rehabilitation there too. This also needs major Federal subsidies.

B. Assessing the Alternatives. How do we assess which of these alternative strategies are *desirable* and which are *likely to occur*? Concerning *desirability* from the viewpoint of older cities themselves, those strategies that produce the greatest upgrading or rebuilding would be

best. They are core-area clearance plus all-out renewal, and residential core upgrading. Both of these strategies require high-level new housing production, major Federal housing aids, and some type of Federal program for long-term-development finance like urban renewal. Thus, *it is clear that major Federal subsidies are needed for city renewal.* Whether they will be politically attainable in a suburban-dominated Congress is a question others can answer as well as I can.

A crucial problem with any desirable strategy is: how can we restore strength of housing demand to older city neighborhoods—demand from households with adequate financial resources? I can see only four major methods: (1) clearing large enough areas to create wholly new environments attractive to middle-income households, (2) dispersing some of the poor from cities to suburban areas enough to dilute their negative impact upon middle-income demand within cities, (3) increasing the incomes of low-income households through subsidies of some kind so that they are no longer low-income, and (4) choking off new suburban growth enough to generate housing demand in cities because of a housing shortage. The second and fourth of these possibilities are politically difficult to attain—and the first and third are extremely expensive.

This does not mean there cannot be some successful rehabilitation in cities. It can occur in areas that have enough locational amenities to attract households with money into spontaneous upgrading, as around Rittenhouse Square in Philadelphia. That can happen and is happening. But it hardly offsets the decline in other areas where no such amenities exist. Abandonment and decay continue there because people's basic incomes are not high enough to pay the high minimal cost of decent housing units.

C. The Most Likely Outcome. To put it bluntly, I believe the existing tendency of many large, older cities in the Northeast and Midwest to experience population losses and physical decay—leading to extreme fiscal problems—will continue unabated in the future unless some very significant Federally financed intervention is made to alter this process. But our past experience with such interventions is not encouraging even when they are undertaken. They are usually not large-scale enough to stop the basic processes at which they are aimed, and they are too fragmented in administration to achieve the overall results desired.

Ultimately, we must choose as a nation between two basic methods of accommodating future urban growth and quality-of-life improvement. One is mainly through further suburban expansion—including regional shifts to Sunbelt suburbs. The other requires slowing suburban expansion in order to create in-city housing demands on which a restoration of our older cities can be built. But the restoration of older cities would require somehow mixing their present poor and minority-group residents with middle-class whites. That could occur either by

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dispersing the poor out of central cities to make room for new middle-class environments there, or by having both groups live close together within the restored central cities.

In contrast, further suburban growth allows continued spatial segregation of housing by both income and race. I believe Americans will overwhelmingly prefer the latter pattern, and will politically oppose any major changes in it.

Furthermore, the shift of both households and business firms from high-cost, relatively obsolete older Northeastern and Midwestern cities and metropolitan areas to much lower cost, more modern, newer Southern and Western cities is a desirable form of economic adjustment. It moves the nation towards a much more efficient long-run use of resources, however unpalatable that may be to Northeasterners and Midwesterners. Economic efficiency is certainly not the only goal of public policy. Nevertheless, in my opinion, it would be a serious mistake for the Federal government to provide sufficient fiscal subsidies to older, high-cost cities so they could fully escape the painful process of reducing the excessive wages and services they now provide. True, they deserve some national assistance to help them carry their disproportionate concentrations of poor households. But without strong regional competition from lower cost urban areas elsewhere, they would never be willing to confront and adjust their essentially nonviable accretions of overly high public payrolls, wage levels, and public services. Ironically, the seemingly disproportionate flow of Federal spending to the South and West that these older cities complain about really represents responsibly efficient use of taxpayers' money by Federal officials. It is decidedly not just the dominance of major committees by Southern Senators and Congressmen. Thus, I believe the long-run shift of households and resources from the high-cost upper right-hand corner of the nation to the lower cost bottom half and left-hand edge will continue until regional cost structures are adjusted downward in the former and upward in the latter.

V. CONCLUSION

With all our blaring headlines concerning urban crises, and the well-publicized handwringing of so many big-city mayors and urban experts and columnists, it is easy to forget that the basic process of urban sprawl and development America has been using for the past three decades has been a huge success for the vast majority of our metropolitan-area households. That is true even though this process also generated massive problems in older inner-city areas. Why should people who have benefited from this system, and do not suffer from its ills, change it—when they form the preponderant majority in our majority-oriented political system?

That is why I believe the basic tendency for most older cities to lose population and suffer deterioration and fiscal difficulties will continue. We will keep on accommodating most upgrading through suburban and nonmetropolitan growth, rather than restoration of

older cities. Undoubtedly, there will be some new Federally financed efforts to aid in rehabilitation and city restoration. They may even be large-scale and expensive. But they will be far too small to stem the tide—even though they may cause showcase improvements in a few neighborhoods and cities.

I recognize that this discussion has greatly oversimplified the immense complexity and variability among communities relevant to the future of our cities to the year 2000. Moreover, I can perhaps be accused of fostering a self-fulfilling prophecy—though that criticism grossly overestimates the influence of my views. True, I have not been overly optimistic about the future, because I have chosen to *forecast* what I think will actually happen—rather than *exhorting* people to behave in some desired way. But I have always tried to tell the truth as I see it about urban affairs. I hope my remarks can at least serve as a start for a fruitful discussion of the future of our older cities up to 2000.

MARTIN MEYERSON

Martin Meyerson assumed the presidency of the University of Pennsylvania in 1970. Educated at Columbia and Harvard, President Meyerson first came to Penn from the University of Chicago in 1952. He went to Harvard five years later as professor of city planning and urban research, and, while there, became the first director of the MIT-Harvard Joint Center for Urban Research. He moved to Berkeley in 1966 as acting chancellor and then to the State University of New York at Buffalo in 1966 as president.

Throughout his career, President Meyerson has played an active role as member or head of public commissions and private foundations here and abroad. He is the recipient of several honorary doctorates and of many other awards, and he serves as a director for several of Philadelphia's best known cultural and commercial institutions. He is the author or coauthor of four books on urban affairs.

Comments

Martin Meyerson

President of the University of Pennsylvania

Anthony Downs is one of our most perceptive analyzers of urban America and one of our most fertile proposers of urban policy. Alas, I did not have his paper ahead of time and thus am commenting on what I have just heard.

We have always had a certain irreverence for authority in this country. That irreverence is a wonderful feature of our national character, but it can reach the point where we take it for granted that anybody in a position of responsibility or authority is suspect. That phenomenon exists in cities, in government, and, of course, in universities. Few in major cities now become second-term elected officials and, for that matter, apparently in the nation. Almost before a candidate wins an election, we are willing to assume that he or she is flawed. This attitude toward authority has led to a tremendous reduction in risk-taking and a failure of nerve and has ultimately injured the city.

Cities have been hurt in other ways as well. There is a suburban dominance in American national politics today. The one man, one vote decision designed to redress rural imbalance has led less to the protection of cities than to the dominance of suburbs. Further, the steady move to the suburbs by the cities' more prosperous residents and activities has impaired the cities' ability to raise revenue. Thus, because of suspicion of authority, because of a new political constellation, and because of continued demographic changes, civic leadership to overcome some of the difficulties of urban America has been hampered.

With regard to some of Anthony Downs's concerns, our cities, like our economy, exist in a market setting. We should try to understand how our cities operate and might operate in this setting. My preferred mode of operation is for government to simulate the market, and to stimulate it.

Many declining older cities in the Northeast and Midwest exist in a national marketplace of cities. These older cities often have built up high costs of government operation and of doing business in the private sector. The shift of resources to cities in other sections of the country acts as a corrective through competition. (For example, Houston versus Newark.) Of course, many of these same older cities have been saddled with the responsibility for poor and dependent

populations. To that extent, they deserve financial aid from the rest of society, and as I shall note later, they are getting it in certain ways. But the extent of the aid should not be so great as to preserve inefficiencies and rigidities, such as exorbitant municipal wage rates. Striking a balance is difficult. But the nation is a marketplace of cities and we should ask the question, how can we best use public action to preserve and improve the old while developing the new.

When I have been asked by political figures what actions to take to help solve the problems of cities, I emphasize as I have said that government mostly should simulate, and stimulate, the marketplace rather than invest in large public works programs. I shall suggest specific ways for such actions to take place.

For example, it is possible for the Federal government to establish for housing, as it did in agriculture, an ever-normal-granary policy. It should be recognized that housing represents not only the largest single expenditure made by any household but that it represents, or should represent, the largest single investment of investors. Private investors have not found housing attractive because it has been so subject to the vagaries of the business cycle. Since housing is the largest single investment made by households, it is the first to fall off during a period of economic ebb. In such periods people continue to live with parents or in the old house; they remain where they are and do not buy or rent new dwellings. With fiscal policies, credit policies, and other policies that correspond to the government stance I recommend, the ever-normal-granary concept could stimulate the private housing market. Such a policy could lead us away from the feast-or-famine habit that is more marked in housing than in any other major business activity in our country. Such a policy would also enable the housing industry to use technological opportunities which it does not now take advantage of. It is possible by government action to stimulate more extensive housing investment from the entrepreneur and housing choice and movement from the consumer.

On another issue, without fully realizing what we have done, we have in many ways federalized welfare payments so that we have eliminated some of the differences for this expense in varying parts of the country. In the literature on urban reform there are still a great many statements on the importance of federalizing welfare. But if most welfare programs are carefully examined, it can be seen that in the past years many programs have in fact been brought under the jurisdiction of the Federal government. There is still much to be done on this score.

However, with regard to equalizing expenditure variations in the nation as they affect our cities and metropolitan areas, we have not acknowledged the tremendous differences in Federal spending among different areas. As we become more aware of these practices, we should discourage the Federal government from promoting such vast differences. Philadelphia, the major cities of the Great Lakes, and

other metropolitan regions get back perhaps 70 cents on the tax dollar. This is in comparison to the major cities of the West where as much as twice that amount is returned for each tax dollar. It is ironic that New York, whose citizens often led the way in calling attention to depressed areas elsewhere in the country, gives a considerable portion of its taxes to pay for services elsewhere in the country. Such reallocation, while sometimes necessary, has not always proved wise. It is important for us to recognize that reallocations take place and to assess the most desirable patterns of each reallocation.

We all recognize the political inability of center cities to resist raises in costs and expenditures in the service area; including those for schools. In some cities, there now exists a very significant difference between what the city will pay and what private enterprise will pay employees, with private enterprise, in a reversal of the usual practice, offering less than municipalities. Moreover, pensions in the public sector have often increased beyond the future ability of the cities and their citizens to pay. It is very hard for elected officials to overcome the political pressures of requests for lavish pensions since typically it is not the incumbent who will pay those pensions but his successors in years to come. Yet interestingly in this case, too, a certain market adjustment is taking place. For there are some pressures for equilibrium in the quasi-markets that exist in municipal and urban life. For example, in certain cities during the past year, there have been pressures for standardization in municipal employee pensions so that these pensions will resemble what the private sector would ordinarily offer.

I wish now to present a few instances of what can happen when imagination about urban problems and understanding of the situation of cities come to the fore and when there is less attachment to vast institutional efforts.

... A new effort under way in New England and elsewhere concerns the placing of criminals in foster homes, a remarkable experiment particularly for youthful offenders who are not yet repeaters. Instead of being put into a difficult jail environment, young violators of the law are placed in a situation that resembles the household most never had a chance to experience. Samaritans, of course, are needed to take on such a task and the results of the program are not yet in. But in our Bicentennial year, we ought to remember that such activity represents the best of our country's history: the history of a people who were willing to take on a shared responsibility, whether to raise a barn or to help the poor or to be a good neighbor.

... In employment, other changes are taking place that make me hopeful. Jesse Jackson, an extraordinary man who some view as among the most militant of black leaders, is helping to develop a national effort on behalf of a work ethic, leaning on faith in the ability of people to change their situation.

... With regard to investment and employment, we have not been

experimental enough. I do not advocate abolishing the minimum wage, if for no other reason than I think it would be politically impossible to do so. But I am not adverse to suggesting that the government should provide subsidies to those organizations which hire at the minimum wage teenagers who are essentially in the learning process. The gap between the worth of the young person to the enterprise and the level of the minimum wage could be viewed as a learning subsidy. Such a policy should be politically possible and would have considerable advantage, since it could act as a hiring incentive for the young who perhaps of all groups have suffered the most from unemployment, especially among minorities.

I have talked about the failure of nerve, a failure which applies not only to government but to private enterprise and its role in the city where there is hesitation to locate a firm or put up housing or take any significant chance. A story I am fond of applies here. A young man goes to work for a development firm in Texas, is sent out on his first job, and then calls back to the firm. He is asked, "What is your news?" and replies, "Well, let me give you the good news first. That property we wanted to get—instead of \$100 million, it is \$80 million." "That is great, that is wonderful," his associate replies. "But what is the bad news?" The young man answers, "The bad news is that they need \$10,000 cash." I tell this story because it has increasingly been assumed that if investment is to take place in urban areas, it has to be risk free. But investment should not be any more risk free in the city than elsewhere; conversely, we ought to make sure that it is not vastly more risk free to invest outside the central city as it sometimes is today.

I wish to add a special point. I think various coalitions are forming—nationally, in the core of cities, in urban areas. These coalitions of blacks, and whites, of various income and other groups, need help and they need leadership that ought properly to come from the White House. I do not, however, mean to suggest that leadership and aid should come primarily through added Federal programs, but rather to suggest that they should come through the stimulus of ideas that the office of the President can offer. I have an example of how such change, through stimulation, can take place.

There was a serious epidemic some years ago in Charlotte, North Carolina. The City Council, not knowing what to do, enforced the housing code. The ordinance was enforced by a coalition of almost every group in Charlotte.

Most of the substandard housing was in black areas, and, as the code was enforced, the owners of these properties tried to conform with the ordinance although it was difficult to do so. Rents went up, but to the astonishment of some observers did not go up by large amounts. Something else occurred. Houses were torn down if it was not worthwhile for the owners to keep them in operation. Tearing down houses gave the owners fallow land. People do not want land to lie

fallow; they want to use it, and so there was pressure to build. New buildings, housing, and businesses were constructed in slum areas. Further, something else happened as the result of what I regard as appropriate government as stimulator. A number of builders decided that if people were going to be displaced in the city by the new construction, new houses should be built on the city outskirts. Hence a great deal of housing was constructed; and in one year, on the fringes of Charlotte, more new housing was built and occupied by blacks than in almost any other metropolitan area in the United States. Some of it, of course, was poorly constructed, but some of it was well done. The rents were higher than people had paid in the slums, but many slum dwellers were able to pay them. The suburbs flourished; the center city flourished. If it is true that both were expanding in a growing area—not at the expense of each other—it is also true that they were flourishing because there was a coalition behind a program of appropriate government stimulus.

Thus, I return to the point I made at the beginning of my comments to suggest that government has an important role to play as stimulator. But leadership and risk-taking are needed. All of us have a role to play in reactivating our own ingenuity in using cooperatively both private and public resources. If any message comes from our Bicentennial, that might be as good as any to guide us as we enter our third century, and do so as an urban nation.

Finally, I do not want to close these comments without giving very special thanks to Anthony Downs for the thoughtful warnings in his paper.

ANITA ARROW SUMMERS

Anita Arrow Summers, Research Officer and Economist at the Federal Reserve Bank of Philadelphia, was trained in economics at Hunter College, the University of Chicago, and Columbia University. Before joining the bank's Research Department in 1971, Mrs. Summers lectured at Swarthmore and served as a consultant to the Fels Center of Government at the University of Pennsylvania.

As member and then head of the Research Department's urban section, Mrs. Summers has written mainly on issues in the financing of education and the funding of municipal government. Active in civic affairs, she serves on the board of Philadelphia's watchdog Committee of Seventy and is a director of the Fellowship Commission. She recently finished a 3-year tour as a director of the Citizens' Committee on Public Education.

DONALD L. RAIFF

Donald L. Raiff, Economist at the Federal Reserve Bank of Philadelphia, was trained at the University of Dayton and at Ohio State. He joined the Research Department in 1972 after a year as Stonier Memorial Fellow of the American Bankers Association.

Mr. Raiff specializes in monetary theory and economic forecasting, and he has published several papers on these subjects in the bank's *Business Review*. Since 1973 he has lectured on money and banking at Temple University.

The initial sections of the following presentation—on revenues and expenditures—were prepared by Anita A. Summers, the sections on accounting procedures and estimates by Donald L. Raiff, and the final section on structural realignment by Anita A. Summers. Nonna Noto did the basic research work on this project, with Mary Hinz and David Fellner.

The Fiscal Stance of Philadelphia

Anita A. Summers and Donald L. Raiff

Like many other cities in America, Philadelphia is concerned about its own fiscal health. Although the City budget is projected to show black ink this year, its current surplus may not be large enough to cover past deficits. The School District has a separate budget; but it shares the property tax base with the City, and it faces an even larger deficit for fiscal 1977 than was anticipated earlier.

Over the past several years, tax increases and transfers from Federal and state governments have boosted Philadelphia's revenues. But inflation rates and levels of service have risen too, and Philadelphia has been increasing its real expenditures at an average annual rate of 4 to 6 percent. Despite several changes in accounting practice, Philadelphia now finds itself depending more heavily than before on short-term borrowing to keep up with its obligations. The City budget has seen some easing recently, but there's no relief in sight for the School District.

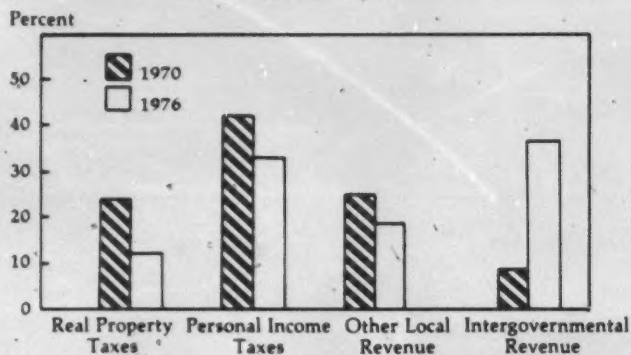
And so the questions: How did this budget situation develop? And how can the cost of municipal services be brought under control or revenues expanded?

LOCAL REVENUES SLUGGISH SINCE 1970

The City and School District together have increased their annual revenues by \$700 million dollars since 1970. Of that increase, the lion's share has come by transfers from the Federal and state governments—70 percent for the City, 63 percent for the School District. In fiscal 1970, less than 9 percent of City revenues came from outside sources. But by fiscal 1976 the figure was up to almost 37 percent (see Figure 1). This development should be regarded as a measure of changed perceptions about who bears the responsibility for the functions that city government performs.

Over the same period, School District revenues have shifted in the same direction but not as dramatically: the intergovernmental share of support rose from about 50 percent in 1970 to about 63 percent in 1976 (Figure 2). This shift of 13 percent, against the City's 28 percent, doesn't show that higher levels of government have *less* concern for schooling than for city administration; it shows instead that Pennsylvania has regarded school financing as an object of state responsibility

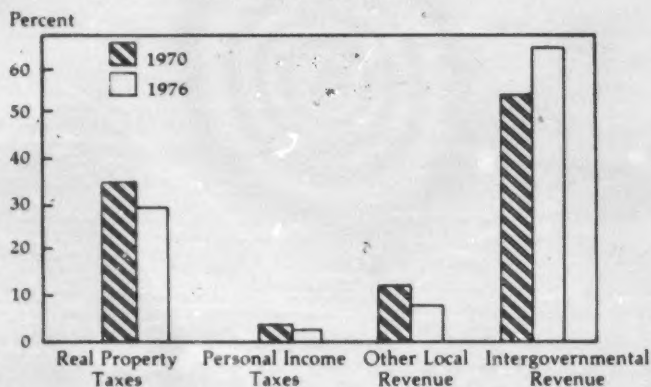
Figure 1
CITY OF PHILADELPHIA:
DISTRIBUTION OF REVENUE BY SOURCE
1970 AND 1976*



*All dates are fiscal years. Changes in budget reporting between fiscal 1970 and fiscal 1976 make precise comparisons difficult.

SOURCES: Annual report and proposed budgets of the Director of Finance of the City of Philadelphia.

Figure 2
PHILADELPHIA SCHOOL DISTRICT:
DISTRIBUTION OF REVENUE BY SOURCE
1970 AND 1976*



*All dates are fiscal years.

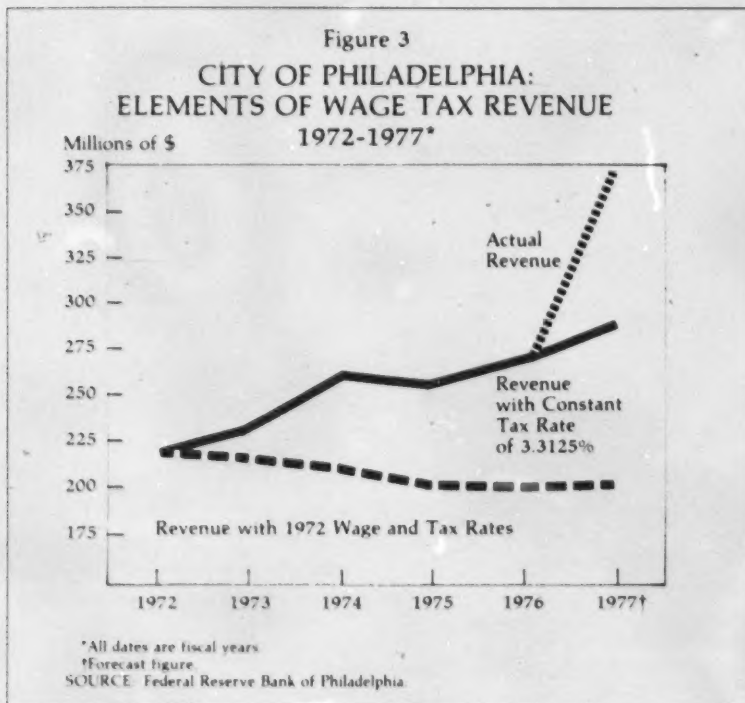
SOURCES: Annual financial reports and budget proposals of the School District of Philadelphia.

for a longer time. Already in 1970 more than half the cost of schooling was being paid through the state government (only 2 percent was channeled through the Federal government). Support for the City still hasn't reached that level, though now Harrisburg and Washington pick up more than 35 percent of the tab.

These transfers of funds from higher levels of government permitted both the City and the School District to get by without raising local tax rates for personal income and real property until quite recently.

Philadelphia instituted a tax on wages in 1940—the first American city to do so. By three decades later, the personal income tax had become the City's largest single revenue source. Personal income tax revenues increase when people are taxed at a higher rate, when more people are taxed (because more people are employed), or when people are taxed on higher wages. For years, Philadelphia had been relying on growth in employment and wage levels to keep taxes up. Wages actually have risen because of inflation; but with employment down (it seems to have stabilized now at a level of about 110,000 below that at the beginning of the decade), the City this year raised its rate.

How all this changed the wage tax revenue picture is shown in Figure 3. The solid line in the middle of the figure represents what the



City has been receiving up to the present and would have continued to receive without the rate change. The dotted line at the top right is the revenue path that's developing now because of the rate hike. The dashed line at the bottom shows what the revenue picture would have been with neither wage increases nor a rate hike. It is clear that wage rate increases have been the major contributor to wage revenue increases.

Why have wage rates risen? Wages can increase because of rises in the cost of living, general inflation, or productivity. In Philadelphia, increases in wage revenues barely have kept pace with increases in the cost of living. What we have here, then, is an expansion in wage revenues for the City based not on the healthy thrust of rising employment or increasing productivity, but on increases in the cost of living.

The School District, unlike the City, gets a large part of its revenue from taxes on real property. And this property tax, as administered, is notoriously inelastic, in that it does not respond to changes in the market values of properties. The record shows that the Consumer Price Index and the market value of housing in this area both climbed about 48 percent over the five years 1970-75. Meanwhile, assessed valuations rose only 17 percent. In other words, the effective tax rate on real property had dropped from 50 percent in 1970 to 40 percent in 1975. The recent 30-percent increase has moved us back, approximately, to an effective tax rate that is consistent with the 50-percent assessment rate of 1970.

In short, the growth in Philadelphia's revenues since 1970 has come from greatly increased support by higher levels of government and from higher taxes. Income tax revenue has risen because of wage inflation and a rate hike rather than from gains in employment and productivity, and property taxes just now have been brought back to about their 1970 effective levels after 5 years of slippage.

REAL EXPENDITURES HIGHER BUT UNEVEN

While municipal revenues have been coming in at a higher volume since 1970, they haven't kept pace with real expenditures (expenditures adjusted for inflation). The City's dollar expenditures are up 119 percent (unadjusted) over this period, and the School District's are up about 82 percent (again unadjusted). Allowing for changes in the price index, the figures are roughly 39 percent for the City and 25 percent for the School District (see Figure 4).

Some City functions saw larger increases than others (see Figure 5), and it's interesting to know why. For example, about two-thirds of the consistent and substantial increases that went to Administration and Other (which includes the Department of Commerce and the offices of the Mayor, Finance Director, and Managing Director) were supported by grant funds that the City obtained through intergovernmental transfers. Among the items paid for this way was the adminis-

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The Fiscal Stance of Philadelphia

Figure 4

PHILADELPHIA CITY AND SCHOOL DISTRICT: PERCENTAGE CHANGE IN PRICE INDEX AND EXPENDITURES FOR SERVICES 1970-1976*

Item	City (percent)	School District (percent)
Nominal service expenditures†	119.0	82.3
Expenditure price index	57.8	45.9
Real service expenditures†	38.8	24.9

*All dates are fiscal years.

†Excludes debt service and employee benefits, which include pensions and social security.

SOURCES: Annual reports and proposed budgets of the Director of Finance of the City of Philadelphia; annual financial reports and proposed budgets of the School District of Philadelphia; Federal Reserve Bank of Philadelphia.

Figure 5

CITY OF PHILADELPHIA PERCENTAGE CHANGE IN REAL EXPENDITURES 1970-1976*

Expenditure Element	Change (percent)
Service	
Administration and Other	96.2
Police	4.0
Fire	3.0
Courts	70.8
Streets	2.7
Recreation and culture	12.0
Health	39.8
Welfare	22.9
Community development	8266.7†
Service average	38.8
Debt service & employee benefits‡	21.4
Combined average	35.0

*All dates are fiscal years.

†Changes in budget reporting between fiscal 1970 and fiscal 1976 make precise comparisons difficult.

‡Includes pensions and social security.

SOURCES: City of Philadelphia *Financial Report for the Fiscal Year 1970 and Supporting Detail for Fiscal 1977 Operating Budget*; Federal Reserve Bank of Philadelphia.

trative cost of Federally funded local employment programs. Thus very little of the increase in Administration and Other came from funds raised locally.

Community Development shows an outlandishly large increase, but that's because the base year saw a very small amount of money allotted to this function in the budget. And this increase is supported entirely by the Federal government. Courts experienced very large growth particularly between 1970 and 1974; and this, too, was supported mostly by intergovernmental revenue.

It's important to observe a few trends. First, no department experienced an absolute decline in real services over this period. Second, if you converted these 6-year rates to annual rates, you would observe that Police, Fire, Streets, and Recreation all grew something less than 2 percent per year over this time (Courts, Administration, and Health grew much more). Third, increases in direct city-to-citizen services have been accompanied by increases elsewhere in the budget. Debt Service and Employee Benefits together have gone up fairly substantially, even in real terms, for several reasons: the City was forced to increase its contributions to the Pension Funds by the Bogen and Dombrowski decisions; the total debt of the City increased by substantially more than inflation; and Social Security payments had to be increased because of an increase in the contribution rate and the extension of the maximum taxable base.

The School District budget also shows larger increases for some functions and smaller ones for others. From 1970 to 1976, the average rise in expenditures for strictly educational functions was about 19 percent (Figure 6). Special Education and Early Childhood Education received a large share of this increase. Both of these were state-mandated programs and were paid for entirely from state funds. The large increase in the Early Childhood program reflects the increase in non-Federal funding that has to accompany Federal support of this program.

Actually, the 19-percent figure gives a distorted picture of the average rise for educational functions, since the number of pupils served by these functions has dropped by 8 percent (the number of instructional staff has increased by 17 percent). Thus, on a *per-pupil* basis, the cost of delivering educational services to students in Philadelphia schools has risen by a good deal more than 19 percent.

There were, further, very large increases in Plant Operation and Maintenance. More had to be paid for fuel, and vandalism raised the outlay for repairs. There was a large increase in Debt Service and Employee Benefits: debt servicing increased by only 9 percent in real terms over the six years, but employee benefits increased by a whopping 95 percent (after correcting for inflation) as a result of various negotiated contracts.

For the School District overall, then, there has been an increase of something like 28 percent in real expenditures. On a *per-pupil* basis,

Figure 6
SCHOOL DISTRICT OF PHILADELPHIA
PERCENTAGE CHANGE IN
REAL EXPENDITURES
1970-1976*

Expenditure Element	Change (percent)
Education	
Early childhood	20.0
Elementary	7.8
Junior high & middle	0.5
Senior high & technical	16.6
Special education	132.8
Education average	18.9
Overhead	
Plant operation & maintenance	61.3
Administration & support	25.1
Overhead average*	41.4
Education and overhead average	24.9
Debt service & employee benefits	43.0
Combined average	28.0
CHANGE IN AVERAGE REAL EXPENDITURE PER PUPIL:	38.1

*All dates are fiscal years.

*Excluding refunds and undistributed items.

SOURCES: School District of Philadelphia *Summary of the Proposed Operating Budget* for the fiscal years beginning July 1, 1971 and July 1, 1976; Federal Reserve Bank of Philadelphia

the real expenditure growth has been even larger—38 percent, or something like 6 percent per year.

What do we see as we look at the City? We see potholes we don't like, crime that worries us, and children less well educated than we wish. Inflation has taken a bigger bite from expenditures than it has added to local revenues. Without the large chunks of intergovernmental revenues that we've been receiving, our services would have declined considerably. Old Philadelphia, like other older cities, is trying to provide adequate levels of service to its concentrations of low-income, high-need people. But because of the nature of the local tax structure, it has had trouble coming up with the money to pay all the bills.

BUDGET BALANCES NOT THE WHOLE STORY

One way to find out how well Philadelphia is doing at paying its bills is to look at its year-end balances. What a quick look shows is that both the City and the School District have been accumulating deficits—the City since 1975, and the School District since 1970, interrupted by the strike-induced adjustments of 1973 and 1974 (Figure 7).

But there's more to the story than these balances tell us. In response to deficits and other developments, municipal officials have made three changes in accounting procedures. And one effect of these changes is to make it harder to compare one year's balances with those of other years. First came the switch to an accounting year which runs from July 1 through June 30; second was the inclusion of only one semiannual debt payment in accounting for fiscal year 1972; and third was the accrual of certain intergovernmental revenues, which started in 1975.

The switch to an accounting year that begins in July was accomplished by the City with an 18-month interim budget for the period January 1968 to June 1969. This interim budget extended over two January-to-June sequences, both characterized by receipt of most of a

Figure 7
PHILADELPHIA CITY AND
SCHOOL DISTRICT
YEAR-END FUNDS AVAILABLE
FOR APPROPRIATION
1969-1976*
(Millions of Dollars)

Year	City† General Fund	City† Operating Funds	School District General Fund
1969	\$14.8	\$25.6	\$(28.3)
1970	21.5	27.1	(2.9)
1971	(36.4)	(28.7)	(5.9)
1972	(6.1)	22.7	(36.2)
1973	3.0	31.7	1.5
1974	14.1	42.3	0.7
1975	(12.3)	11.4	(7.5)
1976	(88.6)	(73.3)	(15.3)

*All dates are fiscal years.

†City data reflect accrual of some intergovernmental revenues in 1972 and thereafter.

SOURCES: Prospectus for City of Philadelphia Water and Sewer Revenue Bonds, August 20, 1976, and annual financial reports and proposed budgets of the School District of Philadelphia.

fiscal year's revenue but obligation of only half its expenses. In calendar year 1968, for example, 72 percent of annual revenue came in during the first six months, but only about 50 percent of annual obligations were incurred. Tacking this 6-month stretch onto the prior 12 months of deficit put the City into the black for the full 18 months, but part of the revenue surge was diverted from increasing

the City's liquid assets to meeting increased obligations. Because the City did not choose to reap the full benefit of its revenue surge in the form of liquidity, it now has to borrow to tide itself over during the fall as it waits for funds to come in during the spring. And the School District faces similar circumstances; it changed accounting years a decade ago.

The City continued to borrow to meet its semiannual debt payment during its lean half year—July to December. It was able to meet the other debt payment out of the spring's revenue bulge. But under pressure of an emerging deficit for fiscal 1972, the City made a second accounting change: it budgeted for only one semiannual debt payment. *No prior arrangement was made for the July payment, which was deferred to the next fiscal year's budget.* And this deferral has been carried forward. Now every 6-month period begins with a semiannual debt payment out of borrowed money, and the next six months are spent repaying that borrowing. Thus the year-end fund position no longer means what it used to, because now it does not reflect the obligations that must be assumed in the next fiscal year to pay off the July debt service.

The third change was the move to accruing revenue—putting it on the books when it's promised instead of waiting until it's received to carry it as an asset. This accounting practice is defensible and may be advisable under certain circumstances. But although it adds numbers to the income side of the ledger, it neither adds to cash flow nor obviates the need for short-term borrowing.

The key point in accrual accounting is the length of time it takes to collect the promised revenue. The City's experience has been uneven (see Figure 8). It took three years to close out receivables accrued in 1971, and 1970 still has \$2.7 million outstanding. On average, 74 percent of receivables are closed out a year after they're accrued. Hence, although the money does come in eventually, the temporary gap has to be bridged with short-term borrowing. Indeed, all three changes in accounting practice have upped the requirements for short-term borrowing.

BUDGET ESTIMATES DIFFERENT FROM ACTUALS

As Philadelphia's fund balances sagged in 1976, estimates of revenues and expenditures turned out to be far off the mark. Fiscal 1976 General Fund revenues were overestimated by \$94.2 million and obligations were underestimated by \$4.3 million (Figure 9). These miscalculations were much more severe than those of earlier years. The overestimate of revenues was four times as large as the average for the previous six years (\$21 million), and the underestimate of obligations was the first in this decade; between 1970 and 1975, on average, the City had *overestimated* obligation formation by \$9.7 million per year.

The accuracy of estimates has an important impact on Philadelphia's

Figure 8
CITY OF PHILADELPHIA
GENERAL FUND REVENUE FROM
OTHER GOVERNMENTAL UNITS
RECEIVABLE AT YEAR-END 1971-1976*
 (Millions of Dollars)

Year in which Accrued	Receivable 1971	Receivable 1972	Receivable 1973	Receivable 1974	Receivable 1975	Receivable 1976
1970	\$4.5†	\$4.5†	\$4.5†	\$4.5†	\$4.5†	\$2.7†
1971	9.7	1.8	0.5	0.5	0	0
1972	—	15.2	2.7	1.3	0.4	0.4
1973	—	—	14.3	2.0	0.9	0.9
1974	—	—	—	20.6	9.6	2.1
1975	—	—	—	—	28.8	7.0
1976	—	—	—	—	—	26.9
Total	14.2	21.5	22.0	28.9	44.2	40.0
Due from Philadelphia Gas Works	9.3	—	—	4.0	5.0	0.4
Total Receivables	23.5	21.5	22.0	32.9	49.2	40.4

*All dates are fiscal years.

†Receivable prior to fiscal 1970.

SOURCE: Prospectus for City of Philadelphia Water and Sewer Revenue Bonds, August 20, 1976.

Figure 9
CITY OF PHILADELPHIA
GENERAL FUND ESTIMATES
AND OUTCOMES
 (Millions of Dollars)
 1976*

Budget Caption	Estimate	Actual†	Effect on Surplus
Revenues	\$800.2	\$706.0	\$-94.2
Obligations	780.8	785.1	- 4.3
Prior year surplus (deficit)	(19.4)	(7.5)	+11.9
Closing surplus (deficit)	0	(88.6)	-88.6

*Fiscal year.

†Preliminary figures.

SOURCE: Prospectus for City of Philadelphia Water and Sewer Revenue Bonds, August 20, 1976.

true budget position and thus on its credit requirements. Two of the methods used to meet these credit requirements are borrowing through the Consolidated Cash Account and deferring payment on current pension promises.

The City uses a common cashdrawer for economy of management—the Consolidated Cash Account. The sources of money in this account can be classified as the General Fund, all other operating funds, and all other member funds including Capital Improvement (loan funds). And the City sometimes borrows money temporarily from one of these three funds to pay off the debt in another.

The cash position of the General Fund has fallen to a \$30-million deficit from the \$57-million surplus of 1970 (Figure 10). By the end of 1976, it was borrowing from other operating accounts, and its current deficiency position ran over the fiscal year ending date for the first time.

Figure 10
CITY OF PHILADELPHIA: EQUITY IN
THE CONSOLIDATED CASH ACCOUNT
1966-1976
Year-End Values (Thousands of Dollars)

Year	General Fund	All Other Member Operating Funds	All Other Member Funds (Including Capital Improvement Funds)	Total
1966 CY	\$25,418	\$8,010	\$51,796	\$85,224
1967 CY	21,732	7,610	54,774	84,116
1969 FY	38,607	11,631	9,399	59,637
1970 FY	57,706	9,817	33,997	101,520
1971 FY	11,051	10,197	109,326	130,574
1972 FY	24,032	29,043	56,133	109,208
1973 FY	24,801	31,842	90,639	147,282
1974 FY	21,558	39,085	42,788	103,431
1975 FY	0	29,230	20,261	49,491
1976 FY	(30,651)	21,921	106,069	97,339

SOURCES: Annual reports of the Director of Finance of the City of Philadelphia and Prospectus for City of Philadelphia Water and Sewer Revenue Bonds, August 20, 1976.

A closer look shows that borrowing through the Consolidated Cash Account is different in different parts of the year. During some quarters, the sum of cash resources of the General Fund, all major operating funds, and all other member accounts except Capital Improvement is not enough to pay the bills. These bills are covered by borrowings from the Capital Improvement Accounts (Figure 11).

Borrowing from long-term sources to pay operating expenses has the advantage that it saves on current interest charges. But it has a

Figure 11
INTERFUND BORROWING THROUGH THE
CONSOLIDATED CASH ACCOUNT
SECOND QUARTER 1975—
SECOND QUARTER 1977
Quarter-End Values (Thousands of Dollars)

Quarter	General Fund	All Member Operating Funds	All Member Funds (Excluding Capital Improvement Funds)	All Member Funds (Including Capital Improvement Funds)
Second Quarter 1975	0	\$29,230	\$37,689	\$49,491
Third Quarter 1975	\$(53,914)	(28,641)	(20,196)	29,835
Fourth Quarter 1975	(88,023)	(56,827)	(44,365)	94,686
First Quarter 1976	(105,144)	(91,203)	(79,177)	20,595
Second Quarter 1976	(30,651)	(8,730)	1,166	97,339
Third Quarter 1976†	(72,831)	(67,515)	(52,302)	59,471
Fourth Quarter 1976†	(50,850)	(29,714)	(12,849)	90,588
First Quarter 1977†	(60,911)	(45,504)	(30,635)	40,646
Second Quarter 1977†	2,625	28,076	42,412	116,650

†Forecast figures.

SOURCE: Prospectus for City of Philadelphia Water and Sewer Revenue Bonds, August 20, 1976.

disadvantage: heavy borrowing could constrain the City's ability to make capital improvements.

Deferring payment on rising pension fund liabilities also keeps credit requirements lower than they would be if the City charged off the full cost of current labor services, which would raise current expenditures; but these costs will have to be paid in the future. Thus, in effect, the City is borrowing against the future.

Estimated pension fund liabilities have risen sharply over the last two years, more sharply than assets, so that the unfunded portion is up to \$722 million from \$566 million. To close this widening gap, the City would have to put even more into the pension fund this year than the projected \$83 million. Allowing the gap to widen will increase future citizens' liabilities to pay for the labor services we enjoy today.

In the face of these deteriorating fund positions and increased financing requirements, the City is adjusting its expenditure plans (Figure 12). Real expenditures are budgeted to increase this year. Our calculations are based on a rise of 2.5 percent in the cost of providing services at last year's levels, but this does not reflect contracted wage increases for uniformed workers. The average expenditure for City services will increase 9.4 percent, down slightly from last year's increase of 10.8 percent. Administration and Other will continue to

Figure 12
CITY OF PHILADELPHIA
PERCENTAGE CHANGE IN
REAL EXPENDITURES
1975-1976 AND 1976-1977*

Expenditure Element	Estimated Obligation Basis 1975-1976 (percent)	Budget Basis 1976-1977 (percent)
Service		
Administration and Other	29.1	16.6
Police	-3.0	5.9
Fire	1.6	0
Courts	5.6	-0.5
Streets	-4.3	-2.2
Recreation & Culture	-0.9	0.9
Health	3.4	-1.7
Welfare	13.5	0.6
Community Development	132.4	90.8
Service average	10.8	9.4
Debt service & employee benefits†	-0.1	20.6
Combined average	8.5	11.6

*All dates are fiscal years.

†Includes pensions and social security.

SOURCES: City of Philadelphia Supporting Detail for Fiscal 1977 Operating Budget; Federal Reserve Bank of Philadelphia.

claim more money, which will be supplied by Federal funds under Community Development, the Comprehensive Employment and Training Act, and other government programs. But except for Police and Employee Benefits, the City departments and budget lines are holding at previous levels or taking some real cuts.

School District officials are operating on a budget that will enlarge their deficit if the schools are kept open all year, though there has been some slight belt-tightening (Figure 13). The outlay for Education and Overhead is budgeted to rise by 4.6 percent compared to last year's 5.4 percent, not counting the effects of inflation. Education continues its real growth rate around 5 percent, so the saving is in Overhead. Within Education, Early Childhood and Junior High are cut or hold the line, while Special Education gets a larger increase than last year. These rises in real expenditures continue despite a reduction in the number of pupils served, so there's a step-up in the growth of average real expenditures per pupil.

The City expects hefty increases in revenue: intergovernmental sources are expected to provide an additional 20 percent, and local tax support is expected to rise by even more (Figure 14). But the School

Figure 13
SCHOOL DISTRICT OF PHILADELPHIA
PERCENTAGE CHANGE IN
REAL EXPENDITURES
1975-1976 AND 1976-1977*

Expenditure Element	Estimated Obligation Basis 1975-1976 (percent)	Budget Basis 1976-1977 (percent)
Education		
Early childhood	18.0	-2.8
Elementary	3.6	4.9
Junior high & middle	-3.8	0.1
Senior high & technical	11.2	4.9
Special education	6.8	13.1
Education average	5.0	5.1
Overhead		
Plant operation & maintenance	6.3	-1.6
Administration & support	6.2	0.5
Undistributed items & refunds	0	1300.0
Overhead average	6.2	3.5
Education and overhead average	5.4	4.6
Debt service & employee benefits	-3.4	7.1
Combined average	3.6	5.1
CHANGE IN AVERAGE REAL EXPENDITURE PER PUPIL:	5.3	6.9

*All dates are fiscal years.

SOURCES: School District of Philadelphia *Summary of the Proposed Operating Budget for the Fiscal Year beginning July 1, 1976*; March 26, 1976, and "Adopted Budget for the Fiscal Year 1976/77," May 27, 1976; Federal Reserve Bank of Philadelphia.

District can point to only relatively slight revenue increases, mainly from the property tax, to go with its estimates of higher expenditures (Figure 15).

Overall the City is looking forward to a better bottom line than the School District—to a \$10-million surplus instead of a nearly \$67-million deficit (Figure 16). Together, those two figures add up to a combined deficit of over \$56 million, down from last year's \$89-million deficit. But information available in the financial releases of the Finance Director's office suggests that the City's projected surplus could disappear, and recent contract settlements could boost the School District's deficit into the neighborhood of \$80 million. The upshot could be a consolidated deficit of around \$90 million—almost unchanged from last year.

Figure 14
CITY OF PHILADELPHIA
PERCENTAGE OF REVENUE CONTRIBUTED
BY ALL SOURCES
1976 AND 1977*

Revenue Source	Estimated Obligation Basis 1975-1976 (percent)	Budget Basis 1976-1977 (percent)
Local		
Real property tax	12.0	14.9
Personal income tax	32.7	33.5
Business activity tax	6.3	6.8
Nontax	12.1	11.5
Local total	63.2	66.7
Intergovernmental		
Federal	22.4	21.9
Revenue sharing	5.5	4.2
Other Federal	16.9	17.7
State	13.9	11.1
Other	0.4	0.3
Intergovernmental total	36.8	33.3
Combined total	100.0	100.0

*All dates are fiscal years. Data include all principal operating funds, except Water, Sewer, and Parking. The Community Development and Grants Revenue funds are also included.

SOURCE: Derived from annual reports and proposed budgets of the Director of Finance of the City of Philadelphia.

STRUCTURAL REALIGNMENT REQUIRED

The outlook for Philadelphia includes inflation that adds more to expenditures than to revenues, no significant increase in the employment base (which would boost income from the wage tax), and no significant increase in intergovernmental revenue. This combination suggests that Philadelphia will have to make some structural realignments in its budgets. The spectre of deficits is likely to remain with us unless some fundamental changes occur. What can we do?

We can increase taxes. Some further taxation beyond the new property tax rate boost might be possible, since the recent property tax increase only corrected for past sluggishness in assessments. Some people argue that raising taxes will induce a substantial loss of citizens and businesses. All other things being equal, that may be true. But it's true also that Philadelphia will lose citizens and businesses if services decline. The trade-off of services against taxes is one that must be considered and estimated.

Figure 15
SCHOOL DISTRICT OF PHILADELPHIA
PERCENTAGE OF REVENUE CONTRIBUTED
BY ALL SOURCES
1976 AND 1977*

Revenue Source	Estimated Obligation Basis 1976 (percent)	Budget Basis 1977 (percent)
Local		
Real property tax	28.5	28.8
Personal income tax	1.6	2.2
Business activity tax	5.6	5.4
Nontax	1.0	0.7
Local total	36.8	37.2
Intergovernmental		
Federal†	3.2	3.2
State	60.0	59.6
Intergovernmental total	63.2	62.8
Combined total	100.0	100.0

*All dates are fiscal years.

†Excludes categorical funds.

SOURCE: Derived from annual reports and proposed budgets of the School District of Philadelphia.

We can reform taxes. The adoption of computerized procedures for automatic reassessment would reduce the sluggishness of the property tax as a revenue source. Improving the equity of the tax might improve its palatability, but whether it would increase revenues remains to be seen.

We can curtail expenditures, perhaps by reducing expenditures for present functions. The data suggest that some curtailment is occurring now in the Department of Streets, while Health and Recreation are just managing to stay the same. Another course is to eliminate some functions altogether. Should the School District, for example, forego some of its functions outside the three Rs? We have no hard evidence that all these functions have been remarkably successful. Philadelphia's educational and financial exigencies may justify reviewing the entire program.

Should some services be transferred to higher levels of government? Surely not on a hit-or-miss basis. Most people regard it as appropriate (efficient) that certain services be voted upon and paid for by the local residents who use them. For example, we generally agree that we should pay for our own fire protection. We raise the taxes locally and pay for the protection locally. It is recognized, however, that the benefits of some services spill over to more people than those who receive the service. Certainly there are many, though not all, who

Figure 16
PHILADELPHIA CITY AND
SCHOOL DISTRICT
BUDGET POSITION
1976 AND 1977*

Budget Caption	Estimated Obligation Basis 1976 (millions of dollars)	Budget Basis 1977 (millions of dollars)
<i>City: Principal Operating Funds</i>		
Revenues	\$809.1	\$1,076.5
Previous year surplus (deficit)	17.1	(73.3)
Expenditures	899.5	993.0
Surplus (deficit)	(73.3)	10.2
<i>School District: General Fund</i>		
Revenues	525.8	548.7
Previous year surplus (deficit)	(7.5)	(15.3)
Expenditures	533.2	600.0
Surplus (deficit)	(15.3)	(66.6)
<i>Consolidated City and School District</i>		
Revenues	1,334.9	1,625.2
Previous year surplus (deficit)	9.6	(88.6)
Expenditures	1,432.7	1,593.0
Surplus (deficit)	(88.6)	(56.4)

*All dates are fiscal years.

SOURCES: Prospectus for City of Philadelphia Water and Sewer Revenue Bonds, August 20, 1976. Federal Reserve Bank of Philadelphia.

feel that the benefits of education extend beyond the individual who receives the educational service. The problem, however, is that public services are not so easily classified by beneficiary. And political jurisdictions may not coincide with benefiting areas. City Line Avenue may separate Philadelphia from Lower Merion politically, but it does not separate those who are benefited by Philadelphia's institutions from those who are not.

Education, welfare, and health are the main candidates for movement to higher governmental units throughout the country. It should be noted that this shifting may not free any given local taxpayer from a tax burden. It depends very much on the characteristics of the local tax that has been used and the characteristics of the new tax that would be used by the higher level of government. It will only be a shift in who is paying how much.

We can increase productivity. Union leaders are for it. Employees are for it. Managers are for it. Everyone is for it. Why does it not occur? In the public sector, we give little incentive to encourage this

development. Reward is perceived to come from size, not reduced size. There is a strong argument therefore for considering what Martin Meyerson talked about today—that wherever possible we ought to consider the use of market forces for performing public functions. Milton Friedman would argue that one should charge users of the Art Museum all that it costs to support an art museum and that some recreation services should be charged to users at full cost. Consumers should purchase their city services, it is argued, as they do their clothing. Those who can afford to get more, get more. Would it be a good idea to legislate, perhaps, that trash must be picked up, but that each of you might choose your own private trash collector? Should we engage in more contracting out of services?

But for other functions, where this direction is not regarded as feasible, we need some form of social engineering. We need to devote resources to radically improving our ability to reduce the ratio of input to output—to reduce the ratio of teachers and materials to achievement growth, to reduce the ratio of sanitation trucks and men to garbage collection. Briefly, we need efficiency analysis in the broadest sense as an integral part of our budgetmaking apparatus. We need to give full recognition in the form of good hard dollar bills to social engineers who would work with the staff of the City and School District, perhaps located in an Office of Economic Affairs. There are some small specks on the horizon here, but I have considerable difficulty seeing them.

On balance, although Philadelphia's fiscal position should be viewed with concern, there are some cheery elements. The City's position has been helped by tax increases. There is some stability in the wage and property tax base ahead over the long run, and some short-run improvements in employment can be expected. Public employee union demands are meeting with more resistance. And the recent attentions to some of the City's financial practices are likely to have a positive effect. But deficits lie ahead for both the City and the School District unless action is taken.

If we continue to shed the functions that are supported from local funding (as we have done with Philadelphia General Hospital, for example, which exemplifies the transfer of functions to higher levels of government); if we search out areas where the private sector, rather than the public sector, can provide the service; if we improve the property tax procedure; and if we work for other transfers to higher levels of government where appropriate—then our fiscal viability might well improve.

This would mean that fiscal design would replace fiscal default. We might then devote our attention to considering how a city might age gracefully, how we might develop more amenities in a city which is less crowded. Exodus might not be all bad.

LENNOX L. MOAK

Lennox L. Moak first served as Philadelphia's Finance Director from 1952 to 1954. After eighteen years as director of the Bureau of Municipal Research and of the Eastern Division of the Pennsylvania Economy League, he returned to his former post as Finance Director in 1972.

Born in Mississippi and educated mainly in Texas, Mr. Moak has spent most of his professional life in New Orleans and Philadelphia. He has been a part of dozens of governmental commissions and has authored or coauthored hundreds of research reports. An occasional university teacher since 1942, he is a contributor to the principal journals in his field and an author or coauthor of six books on government financing. He is collaborating with Lady Ursula Hicks of Linacre College, Oxford on his latest—*Financing the Great Cities of the World*—which will appear in due course.

Mr. Moak long has been active in professional and civic affairs. He is a director of the First Baptist Church of Philadelphia and of the Green Tree School.

Comments

The Honorable Lennox L. Moak
Director of Finance, City of Philadelphia

In general, I find the Summers-Raiff report very useful. I find it very enlightening. Because of the circumstances under which the report necessarily was prepared, I have not had the opportunity to examine some of its basic arithmetic, and this may cause me to have some criticisms later. But the broad outlines I will not dispute, even though I shall call attention to a few things.

I have voiced previously my concern about the classification Administration and Other that appears in some of the tables in the Summers-Raiff report. This classification happens to have the highest rate of growth in expenditures that is reported. My examination of the notes suggests that I would differ very much concerning what is going into that particular classification as constituting Administration costs. Obviously the category embraces much more than ordinary definitions of Administrative costs.

As far as Debt Service and Pensions are concerned, we have increased our costs materially. We have increased our costs in the construction field because the rate of annual increase there has been 11 percent to 16 percent in each year since 1970. This requires a much higher deflator than anything used in this report. Also, interest costs have risen very materially during this period. In viewing this sector of increased costs we should keep these facts in mind. As for the Pension picture, we all know that I was perhaps the principal person behind Dombrowski in the original case. Later I asked him to bring a second case. In the middle of that one I changed uniforms [moving from the Pennsylvania Economy League to the Finance Director's office], and that was kind of embarrassing. However, I think we came out with an even-handed answer. The Dombrowski and Bogen cases were one of the things that confronted the City some four years ago. The results made for a very substantial increase in the costs we should pay each year for pensions (as measured in the report). We have been paying substantial additional amounts; the more recent valuations show a substantial increase in gross liabilities and a substantial increase in net unfunded liabilities—as might be expected in an inflationary economy.

This is a proper showing, although I call your attention to one important fact: we have caused the actuary in the report now in preparation to increase significantly the rate at which salaries and

wages are estimated to increase for the future. In the old valuation, a compound rate of $3\frac{1}{2}$ percent was used; in the current valuation a compound rate of 5 percent is used—which may still be insufficient. Nevertheless, an amount compounded at 5 percent for 40 years has a future value of 1.778 times the same amount compounded at $3\frac{1}{2}$ percent. This helps to account, though it doesn't fully account, for the statement of increased aggregate liabilities set forth in the pension fund valuation. There were also some important increases in pension benefits during that period—some that we deemed advisable to give at the bargaining table and some that were taken away from us by the arbitration process. That process seemingly is endless. I wish it were otherwise.

In regard to revenues received from other governments, I wish to underline the fact that we have aggressively and successfully pursued these! We will continue to do so. One of our best lobbyists is Irvin R. Davis, my chief deputy. He has done a wonderful job of getting additional money out of the state government, and we have had considerable success in Washington. Frequently, where we can get funds determines where the expansion of costs will occur. If we cannot get funds for one purpose but we can for another, if we see a social utility arising out of those funds, we will seek to secure them. We have become increasingly mindful, however, that with certain types of sources, such as the LEAA [Law Enforcement Assistance Agency], the old game is played in which they give you 100 percent funding the first year, 75 percent funding the second year, 50 percent the third, and then 25 percent, and thereafter you're in for the total amount. We can no longer afford these kinds of gifts.

Attention has been directed to three changes in accounting procedures. Two of these occurred before my return to City Hall in 1972—the decision to change the fiscal year (1967) and to change budgeting for payment of the July 1 installment of debt service (1971). The third decision, to change from cash to accrual accounting for earned revenues from other governmental units, was made in 1975. In the aggregate, each of these decisions afforded a temporary advantage by providing a means of delay in revenue adjustments for a period of one year. On a long-term basis, the revenues had to be increased and the City is obliged to pay interest upon the additional funds required temporarily within each fiscal year.

In respect to the third change, I found myself between the devil and the deep blue sea. To continue a system which failed to recognize these receivables as assets for purposes of determining surplus or deficit and fund condition constituted a serious understatement of assets. To modify the system would inevitably bring criticism of "budget gimmickry." I chose the course of change.

A comment has been made about productivity. I am in favor of motherhood, church, and God. But current emphasis on productivity bothers me—not because of the concept itself but because some

promote it as if it were a new discovery. It's the latest fad phrase in budgeting, along with zero-based budgets. In 1945—and these come in regular 10-year intervals—the Hoover Commission assured us that if we would just adopt a performance budget all up and down the line, all of our problems would be solved. Ten years later that was passé. In 1955 we were assured that what we needed to do was to arrange everything by programs so that we could see what we were spending and these programs would conceivably be much better. Results would be perfect, and all our problems would be solved. In 1965, it was PPBS [Planning Programming Budgeting System], with emphasis on the BS. And now we have new fad terms—'zero-based budgeting' and 'productivity'.

It's a nice fad, but we have productivity—very real productivity improvements in this city government. The most significant local example is one started with Joe Clark in 1952. A tremendous decision was made here concerning staffing for fire protection. We had 3,300 firemen; we decided we could run the town on 3,000. Today we have about 2,950. The hours have been reduced from 48 to 42. The occupied area, the developed area of Philadelphia, has increased by something like 40 percent and we are still fighting fires—with a vastly more efficient use of manpower and much more effectively than then. But you don't talk too much about this.

When you're at the negotiating table or at arbitration, you work quietly. Mr. [Richard G.] Gilmore, whom I see sitting down here, worked like mad on the Board of Education during his period for more productivity. He couldn't afford to talk publicly about it and sometimes he was afraid to talk privately. But it was going on. I welcome the pressure. It is good for those of us in public service. But I don't want anybody to conclude that because we don't say very much about it, we are not quite cognizant and making moves.

The interpretation widely given to the pending closing of Philadelphia General Hospital is wrong. Fundamentally, the change was one of moving toward productivity, toward helping out community institutions and at the same time helping out the City and the state to improve health programs. We really are in a posture here that PGH is an anachronism. We made a policy decision after a budget debate within the Administration—a very carefully closed debate. We made an announcement. We have had a lot of criticism from people who thought we had not made enough plans in advance. We deliberately did not engage in detailed planning beforehand because had we done so, we never would have closed PGH. Too many people would have been in on the act, the pressures for maintenance of PGH would have built up, and we would have been defeated.

So far as the overestimation of revenues is concerned, I want to make it clear that in an \$800-million revenue program, I missed the estimate by \$30 million for fiscal year 1976, or 3¾ percent. This was for a variety of reasons—some understandable and some not. The

other \$65 million of difference was laid out as clearly as anybody could lay it out—in the budget message, presentation to City Council, briefing the press—to anybody who wanted to know about it—the *Philadelphia Magazine* to the contrary notwithstanding. John Bunting was nice enough to write a letter without any prompting from City Hall making it clear that the banks were not conned into a position. They knew precisely what the situation was as far as the \$65 million was concerned. That was a political decision. Political leadership has a right to make political decisions. We have to be careful in our discussions of public administration to differentiate among those things that are technical and those which are political.

As for cash management within the year, we have never spent a dollar for operating costs that was ultimately or will ultimately be paid out of capital loan funds! We are in a totally different posture from New York City, absolutely totally different. This must be understood. We must cease and desist from using any language which leaves any possibility for misunderstanding on this point because the costs to the City of Philadelphia are tremendous. We have a common cash fund, the same as you may have in your house. You don't segregate everything down and say well, I have this money for this purpose and I am going to segregate it; and, if I need some money for another purpose, I am going to the bank and borrow it for that other purpose.

We have the two options fundamentally, only two. We cannot turn back the clock of time, which was started by my late and great friend Dick Dilworth, who changed the fiscal year for the School District, which was followed by the City's doing the same thing. It has been done; we cannot revise the property tax calendar to the point where we can get payments at the beginning of the fiscal year. At least for the time being, we're stuck.

We have a negative cash flow from the first day of the fiscal year until about the middle of March. We make up for this by borrowing from our Consolidated Cash Account. So long as we repay it (with interest) then there is, in my judgment, no inhibiting reason applicable to that type of transaction. Obviously, if we did as New York did, actually expended proceeds of long-term borrowing for current operating costs, we would be committing a serious error. It is my intent, as circumstances permit, to build up the amount of the balances in the capital fund somewhere in the magnitude of \$200 million to \$225 million and hold them more or less at that level. I'm going to do it because never again will I stand at the money window and beg for the privilege of paying 9.65 percent in tax-exempt interest, as I had to last year.

I note with interest the comment in the report about the loss of 110,000 jobs. I note, with even greater pleasure, the fact that the Federal Reserve said some time ago that, by 1980, we would be going back up to the general level of 1972. So I presume the Fed will guarantee that I will have the 110,000 jobs back. I am counting on it. We will have a lot of wage tax from these jobs. I thank you all.

CARLA ANDERSON HILLS

Carla Anderson Hills, Secretary of Housing and Urban Development, studied at Oxford and Stanford before entering the Yale Law School. After finishing at Yale and being admitted to the California State Bar, she served two years as Assistant United States Attorney in her native Los Angeles, joining the firm of Munger, Tolles, Hills and Rickershauser in 1962.

Secretary Hills was called away from private practice in 1974 to head the Civil Division of the Department of Justice. She moved from Justice to her present post in 1975.

Secretary Hills is coauthor of books on Federal civil practice and antitrust law. She is a member of the American Law Institute, a fellow of the American Bar Foundation, a member of the Executive Committee of the Yale Law School, and a trustee of Pomona College.

The Changing Nature of Intergovernmental Relations

The Honorable Carla A. Hills
Secretary of Housing and Urban Development

You have invited me to talk with you about the changing nature of intergovernmental relations.

Ours, we are often reminded, is a three-tiered system of Government.

But, we cannot discuss the changing relationships among the three tiers—Federal, state and local—without considering, first, the changing nature of our national economy. For, in the final analysis it is the state of our economy that dictates how that relationship will work.

As Professor Harold Hill said, in "The Music Man":

"We've got a great band! Splendid uniforms! Now, if we could only afford instruments, we could teach the band how to play."

So the primary requisite is a stable, growing national economy, supported by commercial expansion and productive employment—so we can afford the instruments of intergovernmental productivity.

For, as any student of the urban condition knows, the economic ills that beset a nation strike first and hardest in the poorest centers of our largest and oldest cities. And those centers are the last to feel any effects of national economic upturn.

Indeed, none of us here will forget our recent economic history. We all recall too well that in 1975, the major question mark was whether our national economy would sustain the forward momentum which was then on the cusp of a positive turnaround—from the bleak and depressing 12-month period to a terrifying recession compounded by unceasing inflation.

Inflation stood at 12 to 14 percent. The unemployment rate was about 9 percent. Urban revenues were way down. New York was on the brink of financial failure. Industry was depressed and the housing sector was suffering its worst year in three decades.

Here we are, one year later. The nation and its economy survived—and the delicate health of the economic upturn, which we watched so

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fretfully a year ago, has become stronger and stronger with each passing month.

In one short year we have seen: personal income jump \$83 billion; our Gross National Product grow by \$200 billion; tax revenues of state and local governments rise by 11 percent.

Today, there are three million more Americans working than one year ago—in spite of a tremendous influx of women and young people into the labor market. And inflation has been cut to less than half its former rate.

We have come this far, in my view, not through the magic of a big Federal government save, but through the strong and consistent guiding hand of a pragmatic President—assisted and supported by private enterprise. President Ford has not only proved the soundness of his economic course, he has set the tone for a new national awareness that America's wisdom does not reside entirely in the corridors of Congress—that our states and our cities across our diverse land very often can devise better solutions for their individual problems than can Congress which deals in national statistics and devises grand solutions that too frequently miss the mark.

In short, present dissatisfaction with government is based in large measure on the absence of sound and coordinated intergovernmental action. The great American establishment that means Washington to most people—with its vast array of Congressional committees and subcommittees, pressure groups and official lobbies—has somewhere lost track of the fact that programs for the people can only be judged by how well they serve the people.

The Federal government cannot answer the needs of the people simply by legislating new programs with fancy titles and highflown statements of purpose. Nor can it deliver the promise of America just by throwing money at problems.

It worries me that we still hear calls for the Federal government to subsidize the building of 2.5 million housing units a year. Pursuant to the Housing Act of 1968, this nation subsidized, annually, without regard to the market needs of particular areas, more than 2 million housing starts for three years running—and generated a burst of housing overproduction that we are still trying to work off. In the course of this production explosion our nation abandoned thousands of sound, well-designed homes in our cities and under-utilized roads, utilities, and sewage systems already in place there, as buyers heeded the Pied Piper call of "new is better". Neighborhoods were blighted with row upon row of boarded-up houses.

But the Federal government is what the American people have made it. It has grown to fit the expressed will of the electorate. Many of its functions and many of its agencies have survived the voters and the legislatures which put them into being. Many have outlived their usefulness, yet carry on under the protection of strong special interest groups—or voting blocs—or simply because not enough people cared.

It took a long time, and a lot of legislation to create the present tangle, and it is not going to change overnight, regardless of campaign rhetoric.

Since the start of his Administration two years ago, President Ford has taken steps to improve the focus and delivery of Federal assistance to our states and urban centers. On June 30th, the President appointed a Cabinet-level Committee on Urban Development and Neighborhood Revitalization, which I chair, to undertake a comprehensive review of all Federal programs which affect our urban areas; to consult with local officials and community groups regarding how Federal programs impact on communities; and to propose to him statutory and administrative improvements.

Our initial review of the amassed data quickly confirmed what we already suspected. Over the past half-century, succeeding Congresses have enacted so many separate categorical programs that it defies the ingenuity of anybody to develop a coordinated strategy for a Chicago, a Los Angeles, a Cleveland, or a Philadelphia. In addition, there are so many suppliers of Federal funds with so many different schedules, rules, and regulations that it is a practical impossibility to design an efficient urban plan in or out of Washington that will get the most out of the Federal dollar.

I have reviewed 103 Federally funded programs which affect our urban areas and which carry a price tag of roughly \$50 billion a year. Sixty-three of these are direct grant programs—of which only four are broad block grant programs which give substantial discretion to local officials. The other 59 fund projects are in the narrow categories favored by Congress. The remaining 40 are miscellaneous loan programs. Significantly, local governments are eligible, direct applicants in barely one-fourth of all these programs which primarily affect localities. All other program funds are distributed to the states or to special-purpose local agencies.

I do not wish to flatter a local audience by pointing to the superiority of local leadership over Washington planners, but I believe a brief recap of the HUD experience illustrates the advantage to the city, to the state, to the Federal government, and, not least of all, to the taxpayers, of giving broad discretion with Federal funding.

Before President Ford signed the new Housing and Community Development Act into law in August, 1974, HUD had seven categorical grant programs that now are consolidated under our block grant program—each had its own set of requirements, regulations, and timetables. Water and sewers; urban renewal; open space for park development—all of them well-meaning but without any allowance for greater community needs that might lie outside of the strict specifications of the specified seven categories.

The result was confusion, frustration, and interminable delays—often outlasting local administrations, or missing the moment for effective corrective action.

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To make sense out of this morass, this Administration developed the Community Development Block Grant program. Under the program, large cities and urban counties receive unfettered funds which they spend for their localities' most urgent community development needs.

Regulations have been cut from 2600 pages to about 30 pages; applications from 1400 pages to about 50 pages; and review time from an average of 26 months to an average of 45 days. As compared to 1967, we are now providing twice as much funding to twice as many units of government—and we are doing it with fewer HUD employees. But, most important, we are providing local communities with vitally needed funds—on time and in time.

It is my strong belief that our cities can, and will, move forward if the Federal establishment shifts emphasis from categorical thinking to block grant planning. Then funding is put beyond the narrow perspective of some expert in Washington who cannot possibly grasp the individual differences of the thousand upon thousand of localities across our vast country.

The evidence, in fact, is so strong—that I suggest that a forward-looking approach to Federal grant programs should build on four principles:

First, we should prefer block grants to categoricals for all the reasons I have stated here, tonight—particularly in giving local people more control over the resources that affect their lives.

Second, funding should be provided through the elected chief executive officers of states and localities both to assure coordination in the use of available funds and accountability to the people affected.

Third, citizen participation should be the rule rather than the exception in Federal grant programs, which will increase governmental accountability, the cornerstone of our democracy.

And, finally, multiyear funding should be the rule, so that our communities can plan intelligently into the future and, at the same time, take advantage of timely opportunities to get the most effective return on their available funds.

I do not claim that these four principles are the be-all and end-all for every Federal program. But, I believe that our constituencies would fare a lot better if these became the guiding principles of future Federal program planning.

These principles will enhance the special capabilities of each level of government and enable each level to be more responsive and efficient.

For, although local governments are the best situated to solve local problems, they are the least capable of generating significant amounts of revenue. Eighty-five percent of local revenues come from property taxes, and we know that over-taxation of property only serves to halt land development, or encourage disinvestment. And, while it is the Federal government that has the most efficient means of generating revenues and setting national goals, it is the state government that

brings regionalism to government decisionmaking, and provides a safeguard against inequities in local resource allocation.

In planning for this nation's urban future we cannot ignore the need to integrate the political and economic destinies of our cities with their suburbs. Only the state can accomplish that needed feat of political-physical consolidation.

The state legislature of Minnesota, for example, made possible the Minneapolis-St. Paul Metropolitan Council, which is charged with the coordination of community affairs in the Twin-City area and has substantial responsibility for functions ranging from the placement of low-income housing to the location of sewage treatment plants. And it is by Minnesota state law that the property tax benefits from new commerce and industry in the metropolitan area are distributed among all the communities in that locality. By the same reasoning, it was the State of Indiana which enabled Indianapolis and Marion County to establish an efficient and income-equitable unitary government.

Where we have achieved a real intergovernmental partnership—as we have in some areas, based upon the sheer ingenuity of people at each level—we have seen exciting progress.

That the wind of change is blowing was clearly apparent as our President's Committee travelled to our cities over the past several months: in Boston, we saw an energized downtown, supported both by a Government Center and the recently renovated Quincy and Faneuil Hall Markets; in Baltimore, a new convention center complex; in Annapolis, the reclamation of the harbor market; in New York, the rebirth of the old financial district—and here, in Philadelphia, Independence Mall.

We also saw flourishing neighborhoods—rehabilitated neighborhoods for our low-and-moderate income citizens; middle-class ethnic neighborhoods such as Stirling Street in Baltimore and Manchester in Pittsburgh; and wealthy neighborhoods like Georgetown in Washington, Beacon Hill in Boston, and Society Hill in Philadelphia—each contributing to the economic health and cultural diversity of its city.

It is significant that these triumphs of neighborhood revitalization in all parts of the country—coupled with downtown redevelopment masterpieces—have in common one essential ingredient of success:

All of them have come about through local initiative, local planning and local investment. In each case, the principal role of the state and the Federal government has been supportive, not preemptive.

And by the nature of intergovernmental relations—as they have existed in the past—who would say that any of them might not have been achieved sooner and less expensively if the Federal presence, except in funding and national policy considerations, had been further reduced?

Never having heard that point protested by any group of civic leaders—and certainly by no industry doing business with

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Washington—I submit that these local initiatives we now celebrate as breakthroughs can become standard procedure for our cities if principles such as I suggest are adopted to strengthen intergovernmental capacity to deal effectively with the problems of our cities as they exist today. If we persevere in the old myth that our cities can be run from Washington, all of our cities, not just the older ones, face a very bleak tomorrow. And "Intergovernmental Relations" will become just another government project that failed—expensively.

In the final analysis, what we should hope and strive to achieve in our relationship is a partnership joining all three levels of government with the private sector, without whom no plan devised at any level can possibly work.

Your Philadelphia Mortgage Plan is a prime example of partnership participation in Urban Development and Neighborhood Revitalization. Your consortium of banking, government, foundation, and community leadership—concentrating on one of the essential keys to the economic recovery of deteriorating urban areas—not only says something for the indomitable spirit of this fine old city, but it provides other cities with a needed, positive example that neighborhood reinvestment does work.

Area residents may point with pardonable pride to Philadelphia's neighboring and beautiful Main Line. But, you here tonight can point with even greater pride to Philadelphia's beautiful inner-city Green Line.

Thank you.